The Weekly Market Update – 1/9/23: December Jobs Report Looks Good

Major Indices (Price Returns)	Close	Last Week	Quarter-to-Date	Year-to-Date	Trailing 12-Months	All-Time High	% to High
S&P 500	3,895.08	1.45%	1.45%	1.45%	-18.28%	4,796.56	23.1%
Dow Jones Industrial Average	33,630.61	1.46%	1.46%	1.46%	-7.45%	36,799.65	9.4%
NASDAQ Composite	10,569.29	0.98%	0.98%	0.98%	-32.44%	16,057.44	51.9%
Russell 2000	1,792.80	1.79%	1.79%	1.79%	-20.15%	2,442.74	36.3%
MSCI EAFE (USD)	1,995.78	2.67%	2.67%	2.67%	-14.57%	2,398.71	20.2%
MSCI Emerging Markets (USD)	988.68	3.38%	3.38%	3.38%	-19.75%	1,444.93	46.1%
Bloomberg Commodity Index	108.11	-4.16%	-4.16%	-4.16%	9.02%	237.95	120.1%
Barclays U.S. Aggregate Bond	90.45	1.77%	1.77%	1.77%	-13.63%	112.07	23.9%

Source: FactSet

The final employment report of 2022 showed jobs gains, higher labor force participation, and decelerating wage growth. This led to gains in U.S. equities, contributing to a positive (+1.4%) first trading week of 2023 for the widely held, large-company S&P 500 index. On 1/6/23, the Bureau of Labor Statistics (BLS) reported December employment data. The U.S. economy created 223 thousand (K) net new nonfarm payrolls in December 2022, which exceeded the 200K FactSet consensus estimate. While monthly jobs gains decelerated in late 2022 (average monthly jobs gain of 247K in 4Q22 vs. +366K in 3Q22), the report reflected a still-strong labor market, in our view. In 2022, for the full year, the U.S. economy had an average monthly jobs gain of 375K. Also in December, the labor force participation rate (people eligible to be employed as a percentage of the population) ticked modestly higher to 62.3% from 62.2%. This was the highest since August 2022 and reflected new entrants (either recent college graduates or unemployed people returning to search for work) to the employment population. The participation rate remains below the pre-pandemic level of 63.4%. Finally, wages, as measured by average hourly earnings (AHE), increased 4.6% year-over-year (Y/Y) in December 2022. This was down from a 4.8% Y/Y increase the prior two months, and was the lowest wage growth rate in 16 months (since August 2021). Investors viewed the December labor data as a “Goldilocks” (not too hot, not too cold) report, and that fueled market gains. The rapid pace of Federal Reserve Bank (Fed) interest rate hikes (the Fed controls short-term interest rates by setting a range for the overnight bank lending fed funds rate) in 2022 was designed to ease inflation pressure by slowing economic activity. One risk the Fed faces is that raising rates too high in a short period of time could cause a rapid economic slowdown and even recession (a significant decline in economic activity). While higher rates have created challenges for the housing sector, the overall economy continues to create new jobs. In addition, the moderation in wages suggests that inflation pressure from wages could be easing.

We believe the Fed will continue to raise its fed funds target, but is close to a peak level. The Fed’s first Open Market Committee (FOMC) meeting in 2023 is not until 1/31 & 2/1/23 but then meets again in late March and early May. At the December 2022 meeting, FOMC participants estimated a 2023 year-end fed funds level of 5.1%. Given the prevailing fed funds target range of 4.25% to 4.50%, this suggests that the Fed is likely to contemplate an additional 0.75% (75 basis points, bp) of hikes to the target. Despite the easing wage inflation pressure discussed above, we believe that the relatively strong jobs market will keep the Fed on the 75bp path before an anticipated pause (perhaps at the May meeting). We would not be surprised to see the Fed hike by 50bp at the 2/1/23 meeting and possibly another 25bp increase in March. However, following Friday’s jobs report, the fed funds futures market is pricing in a higher probability of just a 25bp fed funds rate increase in February.

In this second week of 2023, 4Q22 earnings season will begin with just a few reports and investors await Thursday’s December inflation data. According to FactSet, just nine S&P 500 companies are set to report financial results this week, and activity will surge next week. Earnings estimates have dropped over the past two weeks, and the FactSet consensus estimate now reflects an expected earnings decline of 4.1%. On 1/12/23, the BLS will report the December consumer price index (CPI, a widely followed measure of consumer inflation). CPI is estimated to have increased 6.5% Y/Y, down from a 7.1% surge in November, reflecting 6 months of lower inflation rates.

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